[JOINT COMMITTEE PRINT]

EXPLANATION OF PROPOSED ESTATE AND GIFT TAX TREATY BETWEEN THE UNITED STATES AND THE REPUBLIC OF AUSTRIA

PREPARED FOR THE USE OF THE

COMMITTEE ON FOREIGN RELATIONS
UNITED STATES SENATE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

SEPTEMBER 15, 1982

U.S. GOVERNMENT PRINTING OFFICE
98-110 O WASHINGTON : 1982 JCS-34-82

J862-34
S382-28

CONTENTS

	Page
Introduction	1
I. Summary	3
II. Overview of United States Taxation of International Gratuitous Transfers and Tax Treaties	4
A. United States Estate and Gift Tax Rules	4
B. Causes of Double Taxation	6
C. United States Estate and Gift Tax Treaties	7
III. Budget Impact	9
IV. Explanation of Proposed Tax Treaty	10
Article 1. Scope	10
Article 2. Taxes Covered	10
Article 3. General Definitions	11
Article 4. Fiscal Domicile	11
Article 5. Real Property	12
Article 6. Business Property of a Permanent Establishment and Assets Pertaining to a Fixed Base Used for the Performance of Independent Personal Services	12
Article 7. Property Not Expressly Mentioned	13
Article 8. Deductions and Exemptions	14
Article 9. Methods for Elimination of Double Taxation	14
Article 10. Nondiscrimination	16
Article 11. Mutual Agreement Procedure	16
Article 12. Exchange of Information	17
Article 13. Diplomatic Agents and Consular Officers	18
Article 14. Entry into Force	18
Article 15. Termination	18

INTRODUCTION

This pamphlet provides an explanation of the proposed estate and gift tax treaty between the United States and the Republic of Austria. The proposed treaty was signed in Vienna, Austria, on June 21, 1982, and has been submitted to the Senate for advice and consent to its ratification.

The proposed treaty is the first estate and gift tax treaty between the United States and Austria. It is similar to other recent U.S. estate and gift tax treaties, and the U.S. model estate and gift tax treaty. In the case of the United States, the treaty applies to the Federal estate tax, the Federal gift tax, and the Federal tax on generation-skipping transfers. In the case of Austria, it applies to the inheritance tax and the gift tax.

The first part of the pamphlet is a summary of the principal provisions of the proposed treaty. The second part provides an overview of U.S. tax rules relating to international gratuitous transfers and U.S. estate and gift tax treaties in general. This is followed in part three by a detailed, article-by-article explanation of the proposed treaty.

I. SUMMARY

The purposes of the proposed estate, gift, and generation-skipping transfer tax treaty between the United States and Austria are to alleviate double taxation on the estates, gifts, and generation-skipping transfers of citizens and domiciliaries of those countries by modifying the jurisdictional rules of such taxation with respect to these individuals and to prevent evasion of taxes on estates, gifts, inheritances, and deemed transfers. The treaty modifies the jurisdictional rules in two ways.

First, an individual's country of domicile is given primary tax jurisdiction over the estates, gifts, and deemed transfers of its domiciliaries (Article 7). However, real property and business property located in the other country ("situs country") are subject to primary tax jurisdiction in the situs country (Articles 5 and 6).

The second modification is that in situations where both countries under their own domestic laws consider an individual to be a domiciliary, the individual will be treated as having only one country of domicile for purposes of the taxes covered by the treaty. The treaty sets forth several criteria to determine which country is the country of domicile (Article 4).

In situations where both countries retain the right to tax transfers the treaty generally provides for relief from double taxation by the country of domicile or citizenship (Article 9). Where the United States is the country of domicile or citizenship, relief is granted through a foreign tax credit. Where Austria is the country of domicile, relief is granted by Austria exempting the property from tax.

The treaty contains the standard provision (the "saving clause") contained in U.S. tax treaties that the United States retains the right to tax its citizens and domiciliaries as if the treaty had not come into effect (Article 9). In addition, it contains the standard provision that the treaty will not be applied to deny any taxpayer any benefits he would be entitled to under the domestic law of either country or under any other agreement between the two countries (Article 1); that is, the treaty will not only be applied to the benefit of taxpayers.

The treaty also contains standard nondiscrimination provisions and provides for exchanges of information and administrative cooperation between the tax authorities of the two countries to avoid double taxation and prevent fiscal evasion.

II. OVERVIEW OF UNITED STATES TAXATION OF INTERNATIONAL GRATUITOUS TRANSFERS AND TAX TREATIES

A. United States Estate and Gift Tax Rules

1. Taxation of U.S. Citizens and Residents

The United States imposes its estate tax on the worldwide assets of estates of individuals who were citizens or domiciliaries of the United States at their death. The United States imposes its gift tax on all gifts made by U.S. citizens and domiciliaries.

The U.S. tax on generation-skipping transfers was enacted in 1976 to prevent the transfer of the use of property from one generation of the transferor's descendants to a younger generation without the payment of estate or gift taxes. In general, the tax on generation-skipping transfers is imposed when property passes through a trust from persons of one generation to persons of another generation and the transfer is not otherwise subject to estate or gift tax. This generation-skipping transfer tax applies to any property deemed transferred by a U.S. citizen or domiciliary and to certain U.S. situs property deemed transferred by certain nonresident aliens.

A unified tax rate schedule applies to transfers at death, to gifts, and to generation-skipping transfers by U.S. citizens or domiciliaries. The highest marginal rate of tax is 65 percent in 1982, phasing down to 50 percent in 1985 and thereafter. A unified credit against the tax allows the cumulative tax-free transfer of up to $225,000 in 1982, increasing to $600,000 in 1987. In general, transfers to the spouse of the transferor are not subject to tax.

Because the United States taxes U.S. citizens (even if they are not domiciled in the United States) and domiciliaries on gratuitous transfers of property wherever located, double taxation of such transfers can arise when foreign countries subject to tax all transfers of property located within their boundaries. The United States seeks to mitigate this double taxation by allowing the estates of U.S. citizens and domiciliaries to credit foreign death taxes against the U.S. tax imposed on property located abroad. The credit cannot exceed the amount of foreign tax attributable to the property subject to double taxation. In addition, the credit for foreign death taxes cannot offset U.S. tax on property located in the United States. Therefore, the credit cannot exceed the amount of U.S. tax attributable to property subject to double taxation.

No credit is available for foreign gift or other transfer taxes other than death taxes.

2. Taxation of Nonresidents Not Citizens of the United States

Estate tax.—The United States imposes its estate tax on any property belonging to any nonresident not a citizen of the United States

(hereinafter "nondomiciliary" of the United States) that is located in the United States at the time of his death. Special situs rules assign locations or deemed locations to certain property.

Whether tangible property is taxable generally depends on whether it was actually located in the United States on the date of death. Thus, all U.S. real property owned directly by a nondomiciliary is taxable. Generally, tangible personal property located in the United States on the date of death is taxable. The only statutory exception to this rule is that certain works of art on loan for U.S. exhibition are deemed located outside the United States and are thus not taxable.

The physical location of intangible property is generally irrelevant for estate tax purposes. Stock of any U.S. corporation (but not of foreign corporations) is deemed to be located in the United States. In general, debt obligations of U.S. citizens, residents, or entities are deemed located in the United States. Certain bank deposits and certain other debt obligations whose interest is treated for income tax purposes as foreign source income, however, are deemed located outside the United States. The proceeds of insurance on the life of a nondomiciliary of the United States are deemed located outside the United States.

The estate of a non-U.S. domiciliary is allowed certain deductions. If U.S. property is subject to nonrecourse indebtedness, that indebtedness directly reduces the value of the property for estate tax purposes.

Generally, however, expenses and other liabilities—including any personal liability of the decedent that is secured by U.S. or foreign property—are apportioned among the estate's worldwide assets and are deductible only on a pro rata basis. The amount deductible is limited to worldwide expenses and personal liabilities multiplied by a fraction the numerator of which is the U.S. gross estate and the denominator of which is the worldwide gross estate. Nonrecourse debt on non-U.S. property is not deductible.

A charitable deduction is available to the estate of a nondomiciliary only if the recipient of the charitable transfer is the United States, a political subdivision of the United States, or a U.S. charitable corporation, or if the recipient is a trust or other association that will use the bequest within the United States.

Unless the estate shows the value of its worldwide assets, no pro rata deduction or charitable deduction is available. No marital deduction is available to the estate of a nondomiciliary.

The highest marginal tax rate applied to the estates of nondomiciliaries is 30 percent of the value of the U.S. situs assets. A credit allows the tax-free transfer at death of up to $60,000. A limited credit for state death taxes is also available, but there is no credit for death taxes paid to foreign governments.

Gift tax.—Nondomiciliaries are subject to U.S. gift tax only on lifetime transfers of U.S. real property or tangible personal property located in the United States at the time of the gift. Gifts by nondomiciliaries of any intangible property (including stock in U.S. companies or obligations of U.S. debtors) are not subject to U.S. gift tax.

Nondomiciliary donors obtain no marital deduction; they are entitled to a charitable deduction like that available to the estates of nondomiciliaries. The tax rate on gifts by nondomiciliaries is not the estate tax rate for nondomiciliaries (with a 30-percent top marginal rate) but

is rather the rate for gratuitous transfers by U.S. citizens and domiciliaries (with a 65-percent top marginal rate in 1982). No credit for state or foreign gift taxes is available.

Generation-skipping tax.—If the deemed transferor of any generation-skipping transfer is a nondomiciliary of the United States, the generation-skipping transfer tax applies only to property to which an estate or gift tax would apply in similar circumstances in the case of an outright bequest or gift by the nondomiciliary. For example, the deemed transfer of real property located outside the United States by a nondomiciliary would not, were it outright, result in an estate or gift tax, so it would result in no generation-skipping transfer tax. The rate on all generation-skipping transfers deemed made by nondomiciliaries is the U.S. domestic transfer tax rate (with a 65-percent top marginal rate in 1982).

3. Determination of a Person's Tax Status

Under the estate and gift tax regulations (sections 20.0–1(b)(1) and 25.2501–1(b) respectively) a resident of the United States is defined as a person who had his domicile in the United States at the time of his death or at the time of the gift. The regulations go on to state that, "a person acquires a domicile in a place by living there, for even a brief period of time, with no definite present intention of later removing therefrom. Residence without the requisite intention to remain indefinitely will not suffice to constitute domicile, nor will intention to change domicile effect such a change unless accomplished by actual removal." Domicile for the U.S. estate and gift tax law is a matter of Federal law. It is not determined with reference to state law and it does not incorporate any presumption that the domicile of one spouse controls the domicile of the other spouse.

4. Taxation of Certain U.S. Expatriates

The United States generally taxes persons whose surrender of U.S. citizenship had a principal purpose of U.S. tax avoidance more heavily than other nondomiciliaries. The estates of such persons who die within ten years of loss of citizenship include stock in certain controlled foreign corporations owning U.S. property, and are subject to the higher tax rates applicable to U.S. citizens or domiciliaries. These estates (like the estates of other nondomiciliaries) obtain a credit equivalent to a $60,000 exemption from estate tax. Gifts of stock in a U.S. company or obligations of a U.S. entity by such persons are subject to U.S. gift tax, whereas similar gifts by other nondomiciliaries are tax exempt.

B. Causes of Double Taxation

Double taxation of gratuitous transfers can arise for a variety of reasons, including conflicts between the laws of the two countries regarding when a person is a domiciliary of the country, conflicts as to criteria for imposing tax, differences in the basic system under which tax is imposed, and taxation of worldwide assets. Double taxation usually occurs in situations where a decedent either was domiciled in both countries or was domiciled in one country and owned property located in the other country.

Since each country has its own definition of domicile, it is possible that a person could be considered a domiciliary of both countries. As such, his estate would be subject to worldwide taxation by both countries.

When the decedent is considered domiciled in only one country but owned property in the other country at the time of his death, that property is subject to tax in the situs country regardless of the decedent's domicile. Thus, the country of domicile will tax the property, since it is included in the worldwide assets of the estate, and the situs country will tax the property because it was located within its boundaries at the time of the decedent's death.

In both of these situations, unless one of the two countries gives up its right to tax the property or allows a credit for the estate taxes paid to the other country, the estate will be subject to double taxation.

Furthermore, the United States imposes its taxes on its citizens regardless of where they reside. Accordingly, a transfer by a U.S. citizen domiciled in a foreign country that taxes the worldwide estates or gifts of its domiciliaries is likely to incur double tax, once by the United States and once by country of domicile. While the United States would allow a credit for foreign duties imposed in such a case, the credit is available only for duties imposed on non-United States property.

A similar situation exists for gifts where the donor is a domiciliary of both countries or where the donor is a domiciliary of one country and the property which is the subject of the gift is situated in another country. As in the case of estates, the country of domicile will tax the gifts made by its domiciliaries on a worldwide basis and the situs country will tax those same gifts to the extent the property is located within its boundaries. Again, unless one of the countries gives up its rights to tax the transfer or allows a credit for the taxes paid to the other country, the gift will be subject to double taxation. The United States does not give a credit against its gift tax.

Also, some countries, like Austria, will tax not only the estate of a decedent domiciled in that country but also inheritances received by persons domiciled in that country when the decedent is domiciled in another country. In this case both countries might tax the same property.

C. United States Estate and Gift Tax Treaties

The traditional objectives of U.S. tax treaties are the avoidance of international double taxation and the prevention of tax avoidance and evasion. To a large extent, the treaty provisions designed to carry out these objectives supplement Code provisions having the same objectives and modify the generally applicable statutory rules with provisions which take into account the particular tax system of the treaty country. Given the diversity of tax systems in the world, it would be virtually impossible to develop in the Code rules which unilaterally would achieve these objectives for all countries.

Notwithstanding the unilateral relief measures of the United States and our treaty partners, double taxation might arise because of different jurisdictional standards, or because of dual domicile. Like-

wise, if both countries consider the same deduction allocable to foreign assets, double taxation can result.

Another related objective of U.S. tax treaties is the removal of a chilling effect on trade and capital flows caused by overlapping tax jurisdictions.

Early U.S. estate tax treaties attempted to relieve double taxation by providing rules for the determination of situs of assets. Under these treaties, the country of domicile would allow a credit for taxes paid to the situs country. These treaties did not attempt to assign a single domicile.

More recent estate and gift tax treaties eliminate double taxation by granting primary taxing jurisdiction to the country of domicile, and by providing rules to determine a single domicile. The country of domicile then generally allows a credit for taxes attributable to (or exempts from taxation) property taxed by the other country on the basis of situs. In addition, several of the more recent treaties expand coverage beyond death taxes to include gift taxes and the U.S. generation-skipping transfer tax. These treaties grant primary taxing jurisdiction on the basis of situs only for real property and business assets.

In its treaties the United States retains the right to tax its citizens on their worldwide transfers as if the treaty had not come into effect, Double taxation can therefore still arise. This double taxation is generally mitigated by granting a credit for transfer taxes paid to the other country.

The treaties also provide for administrative cooperation between the countries. This cooperation includes a competent authority mechanism to resolve double taxation problems arising in individual cases, or more generally, by consultation between tax officials of the two governments.

Administrative cooperation also includes provision for an exchange of tax-related information to help the United States and its treaty partners administer their tax laws. The treaties generally provide for the exchange of information between the tax authorities of the two countries when such information is necessary for carrying out the provisions of the treaty or of their domestic tax laws.

The Internal Revenue Service (and the treaty partner's tax authorities) can request specific tax information from a treaty partner. It can also provide information spontaneously. This can include information to be used in a criminal investigation or prosecution. The obligation to exchange information under the treaties typically does not require either country to carry out measures contrary to its laws or administrative practices or to supply information not obtainable under its laws or in the normal course of its administration, or to supply information which would disclose trade secrets or other information the disclosure of which would be contrary to public policy.

III. BUDGET IMPACT

It is estimated that the effect of the proposed treaty on budget receipts will be negligible.

IV. EXPLANATION OF PROPOSED TAX TREATY

A detailed, article-by-article explanation of the proposed estate and gift tax treaty between the United States and Austria is presented below.

Article 1. Scope

This Article describes the persons who may claim the benefits of the proposed treaty. The proposed treaty will apply to the estate of any individual person who was a domiciliary of either or both countries at the time of his death. Similarly, the proposed treaty applies to all gifts made by donors who were domiciliaries of either or both countries at the time the gift was made. The treaty will also apply to generation-skipping transfers of deemed transferors who, at the time of the deemed transfer, were domiciliaries of either or both countries.

The proposed treaty will not in any way restrict any exclusion, exemption, deduction, credit, or other allowance granted by the internal law of either country or by any other agreement between them. Thus, the treaty cannot cause any person to be taxed at a higher rate than he would be under the Code.

Article 2. Taxes Covered

The proposed treaty generally applies to taxes on gratuitous transfers imposed by the United States and Austria. In the case of the United States, the proposed treaty applies to the Federal estate tax, gift tax, and the tax on generation-skipping transfers. In the case of Austria, the proposed treaty applies generally to the inheritance and gift taxes.

Austria imposes an inheritance tax on property transferred at death where either the heir or decedent has a residence or customary place of abode in Austria. Similarly, Austria imposes a tax on gifts where either the donor or donee has a residence or customary place of abode in Austria. Otherwise Austria will impose its inheritance or gift tax only when the subject property is located in Austria.

The proposed treaty provides that it will apply to any similar taxes on transfers and deemed transfers that either country may impose after the date of signature of the treaty (June 21, 1982). The competent authorities of the two countries must notify each other of any changes that occur in their respective tax laws and of any official published material concerning the application of the treaty, including explanations, regulations, rulings, and judicial decisions.

As is true of other U.S. estate tax treaties, the proposed treaty does not generally apply to death or gift taxes imposed by state or local governments. However, the nondiscrimination Article (Article 10) applies to all taxes of every kind imposed by the United States, Austria, and their political subdivisions. The provisions relating to exchange of information in Article 12 apply to gratuitous transfer taxes and to all other taxes (including income taxes) imposed by the United States and Austria.

Article 3. General Definitions

The standard definitions found in most U.S. estate and gift tax treaties are contained in the proposed treaty.

The proposed treaty defines the term "United States" to include the States and the District of Columbia but to exclude Puerto Rico, the Virgin Islands, Guam, and the other U.S. possessions and territories. Unlike certain estate tax treaties, the proposed treaty does not include in the definition of the United States the territorial sea of the United States or the seabed and sub-soil of the submarine areas adjacent to the coast of the United States over which the United States exercises sovereign rights for the purposes of exploration and exploitation of natural resources (i.e., the continental shelf).

The treaty defines Austria to mean the Republic of Austria.

The U.S. competent authority is the Secretary of the Treasury or his delegate. The Austrian competent authority is the Federal Minister of Finance.

The proposed treaty also contains the standard provision that unless the context otherwise requires or the competent authorities of the two countries establish a common meaning, undefined terms are generally to have the meaning which they have under the applicable tax laws of the country applying the treaty.

Article 4. Fiscal Domicile

The concept of domicile is important because under the proposed treaty the country of domicile has the primary tax jurisdiction over all property transferred other than the property subject to situs taxation. The threshold test for determining the country of domicile is the domestic laws of each country. However, in those situations where both countries would treat an individual as a domiciliary, the treaty sets forth rules for establishing the country of domicile for purposes of the taxes covered by this treaty.

The proposed treaty provides that a person will be a domiciliary of the United States if he is a "resident" of the United States. Article 3(2) of the treaty states that terms not defined in the treaty are defined by the estate and gift tax law of the country to which the term applies. Since the term "resident," as it applies to U.S. persons, is not defined in the treaty, recourse to U.S. estate and gift tax law is necessary to determine whether a person is a U.S. resident. Under U.S. law, a person is generally a resident of the United States if he had his domicile in the United States at the time of his death or at the time of the making of a gift. (Treas. Regs. §§ 20.0–1(b)(1) and 25.2501–1(b).)

The treaty provides that a person will be a domiciliary of Austria if he has his domicile (*Wohnsitz*) or habitual abode (*gewöhnlicher Aufenthalt*) in Austria.

To provide relief from double taxation where the individual is considered domiciled in both countries, the proposed treaty provides a series of rules designed to establish a single country of domicile for the individual for purposes of the taxes covered by the treaty. The country so selected will then have the primary tax jurisdiction with respect to the worldwide estate of the decedent or with respect to his worldwide gifts, other than real property and assets of a permanent establishment or a fixed base situated in the other country. As described below, these rules are based on the concept that primary tax

jurisdiction should be exercised either by the country of nationality, if the dual domicile individual has not been resident in the other country for a substantial period of time prior to his death or the making of the gift, or by the country in which he has his most significant contacts if the nationality test is not determinative.

Under the first of these rules, if the individual is a citizen of one country and not a citizen of the other country and has been domiciled in that other country for less than five years (including temporary absences) during the preceding ten-year period, then the individual will be considered a domiciliary of the country of his citizenship. Under this rule, for example, Austria may not tax the estate or gifts of a U.S. citizen who has been domiciled in Austria for less than five years as if the U.S. citizen were an Austrian domiciliary. (This rule is reciprocal.) If, however, the individual has been domiciled in the country of which he is not a citizen for five or more years out of the ten-year period his domicile for purposes of the treaty would be determined under the tie-breaker rules described below. The five out of ten-year period is shorter than the seven out of ten-year period in the U.S. model treaty.

It is contemplated that this five-year rule will resolve most dual domicile situations. However, if a dual domicile problem still remains after application of this rule, the proposed treaty provides four additional tie-breaker rules to determine domicile. The rules (applied in the order presented) provide that the individual will be considered domiciled in the country (1) in which he had a permanent home available to him, (2) in which his personal and economic relations were closer (center of vital interests), (3) in which he had a habitual abode, or (4) of which he was a citizen. In cases where an individual's domicile cannot be determined by these tests, then the competent authorities of the countries are to settle the question by mutual agreement.

Article 5. Real Property

Under the proposed treaty, real property is one of the two types of property over which the situs country, as opposed to the country of domicile, has primary tax jurisdiction. The other is assets of a permanent establishment or fixed base (Article 6).

The determination of whether an item of property is real property is to be made under the laws of the country in which the property is located. Real property is specifically defined to include:

1. Property accessory to real property;
2. Livestock and equipment used in agriculture and forestry;
3. Rights to which the provisions of general law respecting landed property apply;
4. Usufruct of real property; and
5. Rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources.

Real property does not include ships, boats, or aircraft.

Article 6. Business Property of a Permanent Establishment and Assets Pertaining to a Fixed Base Used for the Performance of Independent Personal Services

Under the proposed treaty, the second type of property owned by a nondomiciliary over which the situs country has primary tax jurisdic-

tion is the business assets of such person's permanent establishment which is located in the situs country and the assets pertaining to a fixed base of such person which is situated in that country and is used for the performance of independent personal services. The real property of either enterprise may be taxed by the country in which it is situated, as provided in Article 5.

The proposed treaty contains a definition of the term "permanent establishment" which is similar to the definition found in recent U.S. income tax treaties, the U.S. model and the O.E.C.D. model.

Generally, any fixed place of business through which a person engages in a trade or business is considered a permanent establishment. A permanent establishment includes a branch, office, factory, workshop, mine, oil or gas well, quarry, or any other place of extraction of natural resources. A permanent establishment also includes any building site or construction or installation project, or an installation or drilling rig or ship being used for the exploration for or development of natural resources, but only if it has remained in the country for more than 12 months.

This general rule is modified by providing that a fixed place of business which is used for certain activities specified in the treaty will not be considered a permanent establishment. These activities include, for example, the warehousing of goods for purposes of storage, display, or delivery, or for processing by another person. They also include maintenance of a fixed place of business for the purpose of purchasing merchandise or collecting information, or for carrying on activities of a preparatory or auxiliary character.

Article 7. Property Not Expressly Mentioned

This article sets forth the general treaty rule that the country of domicile, as determined under the treaty, has the primary tax jurisdiction over the transfers of its domiciliaries, other than the property specifically reserved for situs taxation. The proposed treaty generally provides that property (other than real property (article 5) and business assets (Article 6) located in the treaty country that is not the country of domicile) will be subject to tax only in the country of domicile of the decedent, donor, or deemed transferor. Thus, tangible personal property not connected with a business will be subject to tax only in the country of domicile, regardless of location at the time of transfer or deemed transfer. Similarly, stock, debt obligations, and other intangible personal property not connected with a business will be subject to tax only in the country of domicile, regardless of the identity of any issuer or the physical location of any instrument evidencing the intangible property.

However, this rule of exclusive jurisdiction to tax in the country of domicile does not apply if the domiciliary is a citizen of the United States or (in certain cases) expatriated himself to avoid U.S. tax (see Article 9). Since the United States imposes its tax on the basis of citizenship as well as domicile, there is still the possibility of double taxation if an individual is a U.S. citizen and an Austrian domiciliary. This double taxation is alleviated under the tax credit structure in Article 9.

If the laws of the United States and Austria conflict as to whether a property right or interest falls within either Article 5 (real

property) or Article 6 (business assets), the law of the country not the domicile of the transferor or deemed transferor will govern as to that issue.

Article 8. Deductions and Exemptions

Having generally granted primary taxing jurisdiction to the situs country for real property (Article 5) and business assets (Article 6), and to the country of domicile for other property, the proposed treaty generally allocates deductions for debt on the basis of the relationship (or lack thereof) between the debt and specific property.

The proposed treaty provides that a deduction or reduction in the taxable value of property shall be allowed for debts especially securing real property subject to situs taxation under Article 5. In addition, a deduction or reduction in the value of real property is allowed for unsecured debts incurred for the acquisition, conversion, repair or upkeep of such real property.

For business assets (Article 6), a deduction or reduction is allowed for debts pertaining to the permanent establishment or fixed base. These rules, allowing debts to reduce the value of property they secure or affect, differ from the rules of the Internal Revenue Code and the U.S. model treaty, which provide that only nonrecourse debts specifically reduce the value of a nondomiciliary's property, while other debts reduce worldwide assets proportionately.

To the extent that debt that is deducted from (or that reduces the value of) specific real property or business assets in the situs country exceeds the value of that property or those assets, it is deducted from the value of any other property taxable by that situs country. Debts not deductible under the treaty from the value of real property or business assets are deducted from the value of all other property (described in Article 7), which is taxable by the country of domicile.

Debts not deducted in any of the above ways from the value of property in the country of primary taxing jurisdiction are to be deducted from the value of property liable to tax in the other country.

If a taxpayer deducts any debt in accordance with the above treaty method, he may not use other rules found in the internal law of the United States or Austria to compute other debt deductions. In effect, the nondomiciliary transferor may choose between the treaty rules and the Internal Revenue Code rules for deductions, but must choose one set of rules in its entirety.

Unlike the U.S. Model Estate and Gift Tax Treaty and other recent U.S. estate and gift tax treaties, the proposed treaty does not provide special rules for the deduction of charitable gifts to foreign entities or for a marital deduction. A marital deduction was not considered necessary because Austria's tax rate on transfers to a surviving spouse is low. A charitable deduction was not provided for because of Austria's policy never to permit a deduction for transfers to foreign charities.

Article 9. Methods for Elimination of Double Taxation

The proposed treaty preserves the right of the United States to tax its citizens no matter where they are domiciled. Consistent with the Internal Revenue Code, the treaty also preserves the right of the United States to tax former citizens whose loss of citizenship had as one of its

principal purposes the avoidance of tax, including the avoidance of Federal income tax, but only for a period of ten years following the loss (secs. 2107 and 2501(a)(3)). Thus it preserves the general United States rule of worldwide taxation of citizens and residents. These rules generally do not apply to restrict the credit provisions (Article 9), the nondiscrimination provisions (Article 10), and the mutual agreement provisions (Article 11).

In general, double taxation is avoided because the United States allows a credit for taxes paid to Austria on property subject to situs taxation in Austria and because Austria exempts from taxation property that is subject to situs taxation in the United States.

Under the treaty, the United States is obligated to grant a credit against its estate, gift or generation-skipping transfer tax imposed on a U.S. citizen or domiciliary in two cases.

First, the United States will allow a credit against its tax for taxes paid to Austria on the transfer of property where, under the proposed treaty, the property is subject to situs taxation in Austria (Articles 5 and 6). The credit is to be calculated according to U.S. law, and is not to exceed the U.S. tax attributable to the property.

Second, the United States will grant a credit for Austrian inheritance or gift taxes paid on account of a U.S. citizen's domicile in Austria at the date of his death, gift, or deemed transfer. However, the credit is not available for Austrian taxes imposed on the transfer of U.S. situs real estate or business property taxable by the United States under Articles 5 or 6. Thus, the United States retains primary taxing jurisdiction over real property (Article 5) and business assets (Article 6) located in the United States. Again, the credit cannot exceed the U.S. tax attributable to the property taxed by Austria. The credit is generally not available in the case of a former U.S. citizen whose loss of citizenship had as one of its principal purposes the avoidance of U.S. tax.

In order to avoid double taxation, the United States will take into account in allowing credits taxes imposed by Austria on prior gifts of the decedent where the property is in the taxable estate of the United States.

Austria will eliminate double taxation of its domiciliaries by exempting certain transfers from tax. Real property and assets of a permanent establishment or fixed base, which are subject to situs taxation in the United States as provided for in the proposed treaty, will be exempt from tax in Austria. Moreover, Austria will exempt from taxation property (except real property and business assets located in Austria) previously subject to tax in the United States on a prior gift or deemed transfer. However, exempt property may be taken into account in calculating the amount of tax on any remaining property which is subject to Austrian taxation (i.e., an exemption with progression).

Under the Internal Revenue Code, a claim for credit or refund of U.S. taxes by reason of the payment of foreign death taxes generally must be made within four years from the date the return was filed. The proposed treaty provides a period of limitation during which claims for credit or refund of taxes based on the provisions of the treaty may be made which, in some cases, may be longer than that allowed by the

Internal Revenue Code. It is provided that a claim for a credit or refund of taxes based on the provisions of the treaty must be made within two years from the final determination and payment of a tax for which a credit is claimed under the treaty (provided the determination and payment occur within ten years from the date of the decedent's death, the date of the gift, or the date of the deemed transfer). The competent authorities may extend the ten year limitation if circumstances prevented the determination of the tax within that ten-year period.

The proposed treaty follows the approach of other U.S. estate tax treaties and provides that any refund based on the provisions of the treaty is to be made without interest.

Article 10. Nondiscrimination

The proposed treaty contains a comprehensive nondiscrimination provision relating to all taxes of every kind imposed at the national, state, or local level. (See Article 2(3).) It is similar to provisions which have been embodied in other recent U.S. tax treaties. The purpose of the nondiscrimination provision is to prohibit a country from using its tax system to discriminate against residents of the other country.

Under this provision, neither country can discriminate by imposing more burdensome taxes (or other requirements connected with taxes) on citizens of the other country than it imposes on its own citizens who are in the same circumstances. The provision applies to citizens who are not domiciled in a contracting State. For this purpose, a U.S. citizen not domiciled in the United States is not in the same circumstances as an Austrian citizen not domiciled in the United States, because the U.S. citizen is taxed by the United States on his worldwide transfers and income while the Austrian citizen is not.

Similarly, neither country may impose more burdensome taxation on a corporation wholly or partly owned by individual residents of the other country than it would impose if those owners were its residents.

Article 11. Mutual Agreement Procedure

The proposed treaty contains the standard mutual agreement provision which authorizes the competent authorities of the United States and Austria to consult together to attempt to alleviate individual cases of double taxation or cases of taxation not in accordance with the proposed treaty.

Under the proposed article a person who considers that the action of the countries or either of them will cause him to pay a tax not in accordance with the treaty may present his case to the competent authority of the country of which he is a citizen or resident. The presentation must be made within one year after a claim, under the proposed treaty, has been finally settled or rejected. The competent authority then makes a determination as to whether or not the claim has merit. If it is determined that the claim does have merit, and if the competent authority cannot unilaterally solve the problem, that competent authority endeavors to come to an agreement with the competent authority of the other country to eliminate taxation which is not in accordance with the provisions of the treaty.

The provision requires the waiver of the statute of limitations of either country so as to permit the issuance of a refund or credit notwithstanding the statute of limitations. The provision, however, does not authorize the imposition of additional taxes after the statute of limitations has run.

The competent authorities are also directed to resolve any difficulties or doubts arising as to the application of the convention. Under this authority, the Internal Revenue Service from time to time issues rulings defining terms in a treaty.

The treaty authorizes the competent authorities to communicate with each other directly for purposes of reaching an agreement in the sense of the mutual agreement provision. It also authorizes them to meet together for an oral exchange of opinions. These provisions make clear that it is not necessary to go through normal diplomatic channels to discuss problems arising in the application of the treaty and also removes any doubt as to restrictions that might otherwise arise by reason of the confidentiality rules of the United States or Austria.

Article 12. Exchange of Information

This article forms the basis for cooperation between the two countries in their efforts to deal with avoidance or evasion of their respective taxes and to enable them to obtain information so that they can properly administer the treaty.

The proposed treaty provides for the exchange between the countries of tax-related information and information necessary to carry out the provisions of the proposed treaty or the tax laws of one of the countries, insofar as its taxation is not contrary to the proposed treaty. The exchanges are to be both spontaneous and upon request. The information is not limited to information about the transfer taxes covered in the proposed treaty; this exchange of information provision applies to all taxes (including income taxes) imposed by the United States and Austria. This provision does not apply to political subdivisions of the two countries, however.

Information exchanged is to be treated as secret in the same manner as information obtained under the domestic laws of the receiving country. Such information, however, may be disclosed to persons involved in the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to, or the oversight of the administration of the taxes to which the Article applies. Accordingly, it is clear that the appropriate committees of Congress and their agents, in the exercise of their oversight responsibilities, could have access to information obtained under the treaty.

The proposed treaty contains narrow limitations on the obligations of the countries to supply requested information. A country is not required to carry out administrative measures contrary to its law or administrative practice or the law or administrative practice of the other country, to supply particulars not obtainable under its laws or in the normal course of administration, or to supply information that would disclose a trade secret or the disclosure of which would be contrary to public policy.

The proposed treaty provides that a country receiving a request will endeavor to obtain the information requested as if its own taxation were involved. Upon specific request of the competent authority

of the other country, a requested country is to produce depositions of witnesses and authenticated copies of original documents to the extent obtainable to enforce its own tax laws.

The proposed treaty allows each country to use the mails to deliver documents to private parties in the other country. The treaty does not override U.S. or Austrian laws that may require a different form of delivery, however.

Article 13. Diplomatic Agents and Consular Officials

The proposed treaty provides that its provisions are not to affect the fiscal privileges which diplomatic and consular officials enjoy under the general rules of international law or the provisions of special agreements. Moreover, the proposed treaty shall not apply to officials of international organizations or to members of a diplomatic mission or consular post of a third country who are not considered domiciled in either country for purposes of estate, inheritance, gift, or generation-skipping transfer tax liability.

Article 14. Entry into Force

The proposed treaty is subject to the ratification procedures of each country and requires that the instruments of ratification be exchanged in Washington as soon as possible. The treaty will enter into force on the first day of the third month after the month of exchange of instruments of ratification and will apply to estates of persons dying, gifts made, and generation-skipping transfers deemed made on or after that date.

Article 15. Termination

The proposed treaty will continue in force indefinitely. However, either country may terminate the treaty after it has been in force for five years if at least six months prior notice has been given. If terminated, the treaty will not apply to estates of persons dying, gifts made, or generation-skipping transfers deemed made after the December 31 next following the date of termination specified in the notice of termination.

○